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November 23, 1971

MEMORANDUM FOR: MR. KISSINGER

FROM: JOHN H. HOLDRIDGE

SUBJECT: Japanese Prime Minister Sato's
New Lease on Life

At Tab A is a memorandum prepared by Jack Froebe of your staff, revising our estimate on Japanese Prime Minister Sato's political hold on his position. Based on Embassy Tokyo's revised estimate of Sato's political position, Mr. Froebe's memorandum predicts that Sato will almost certainly be able to see the Okinawan Reversion package through the current special session (scheduled to end next month), and that he might also be able to fulfill his hopes of presiding over the Okinawan Reversion ceremonies next July.

This estimate is contingent, however, on Sato's not having to weather additional severe shocks, either from within or without. Sato's ability to hold on until the middle of next year will also depend on his handling of Japan's China policy and the country's current economic downturn. This in turn will strongly influence his ability to insure that Foreign Minister Fukuda succeeds him as Liberal Democratic Party President and Prime Minister.

State Dept. review completed

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Japanese Prime Minister Sato Gets a New Lease on Life

Our Embassy in Tokyo has revised its earlier prediction that Prime Minister Sato might well not survive the year. It now believes he will almost certainly have no problem staying through the Diet action on the Okinawan Reversion package (to be completed within the next month), and ventures that he might even be able to fulfill his hopes of presiding over the Okinawan Reversion ceremonies in mid-1972. The Embassy pegs its prognosis to the assumption that Sato will not be saddled with further shocks such as (a) extremist attacks on Diet during current Okinawan Reversion session of such proportions that Sato would have to "assume responsibility" a la Kishi in the 1960 Mutual Security Treaty session, or (b) any U. S. - PRC agreements emerging from the President's visit that would overleap current Japanese China policy.

The Embassy explains Sato's improved fortunes by:

-- Japanese have pretty much gotten over their initial highly emotional reactions to the series of shocks that began in July, and are adjusting to the results. Particularly in the economic area, they recognize that our New Economic Policy affected other nations as well and that they were not discriminated against. In addition, factional leaders in Sato's Liberal Democratic Party (LDP) do not want to pick up the current responsibility for negotiating solutions to problems raised by our NEP.

-- Sato has shown a resurrected decisiveness in handling Chirep and the textile problem, and has thus deprived his critics of a prime argument.

-- LDP Secretary General Hori has been able to isolate Party dissidents through carrot and stick techniques, threatening Diet dissolution and elections when Party rebels publicly challenge Sato's leadership, while promising sizable campaign contributions to those who accept Party discipline. Together with the above two factors, Hori's effectiveness probably accounts for the LDP's holding intact, as for example on the defeat of the two no-confidence motions in the Lower House of the Diet October 27. (One was against Foreign Minister Fukuda for the Chirep defeat, while the other was against International Trade and Industry Minister Tanaka for the U. S. - Japan textile agreement.)

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Sato's Continuing Challenges

While it is now safe to assume that Sato will ride out the current Diet session on Okinawa, whether or not he can fulfill his ambition of presiding over the formal reversion ceremonies next July is problematical. His survival quotient will probably derive chiefly from his handling of two major problems now facing him -- China policy and Japan's current economic downturn. His success on these two will also affect importantly a third major problem he has before him -- the choice of his successor as LDP President and consequently Prime Minister.

1. China Policy.

Sato is caught between several pressures on China policy -- our China policy; Peking's stiff-arming Sato's attempts to open direct official contacts with it while it manipulates Japanese business and opposition groups*; Sato's desire to maintain relations with the Republic of China (ROC), for which the older conservative LDP mainstream group members have particular sympathy; and the resulting attempts by Sato's political opposition to exploit his dilemma in the context of the choice of his successor.

For the short run, Embassy Tokyo believes that Sato will make no major change in Japan's China policy beyond the recent modifications induced by our own China initiative -- Sato's decision to find a means to open direct governmental contacts with Peking and to set the objective of the resulting talks as the normalization of relations with the PRC. The basic reason cited for the GOJ's delaying further major change is that it still holds its relationship with the U. S. to be the

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cornerstone of its foreign policy, and U. S. policy toward any other country to be the critical consideration in Japan's own policy toward that country. The Embassy bases its estimate, however, on the assumption that the President's visit to Peking will not result in agreements on major substantive issues that would overleap Japanese policy, and that we will not compromise our defense commitment and ties to Taiwan, without which Japan would not feel capable of retaining its relationship with the ROC.

Another factor that would possibly move Sato toward major change in his China policy is inadequate consultations on the President's Peking trip. Should Sato fear our lack of consultation presaged the conclusion during the trip of major substantive agreements bearing on Japan's interest, he might attempt, in order to protect his domestic political flank, to preempt our suspected move by a dramatic initiative of his own.

A final factor weighing on Japan's China policy is Taipei's reaction to Tokyo's current moves in this field. Should the ROC break its recent silence and give vent to its resentment of the Japanese actions (for example by recalling its ambassador or threatening economic retaliation), then the ROC's conservative friends in Sato's LDP mainstream group would find their ability to preserve the Japan-ROC relationship severely undercut.

Embassy Tokyo discounts the Sato Government's seemingly forthcoming statements on China policy during the recent Diet debate as designed to create the impression of flexibility and movement in his policy. (Sato, carefully couching his words in ambiguity, reiterated his position that "China is one," announced that the "PRC represents China," and added that he is willing "to discuss" the 1952 ROC-Japan Peace Treaty, which the PRC demands be abrogated.)

Thus, for the short run the most important outside influence on Japan's China policy will be that of ours. ROC actions also will figure importantly. Peking, however, so long as it continues to insist on its three conditions concerning Taiwan as pre-conditions for direct official contacts with the GOJ, will not be able to induce a change in Japan's policy in the short run -- provided that Sato's hand is not forced by either of the first two factors and that his domestic political position otherwise remains stable. Sato does not on his own seem desirous of making radical departures in his China policy at this point -- given his interest in Taiwan, his preference to keep in tandem with

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our policy, his having gotten domestic criticism on this score at least temporarily under control, and the Japanese preference for moving slowly, cautiously, and only after a new consensus has been developed. He continues, however, to be faced with the problem of keeping the lid on pressures from those in his own and opposition parties, in business, and within his own bureaucracy who are trying to move the government toward rapid expansion of ties with Peking.

2. Japan's Economic Downturn.

Prime Minister Sato's second major immediate problem is bringing Japan out of its current economic downturn. The growth of Japan's GNP in real terms has been very slow since mid-1970: for the current year it is projected at only 5.5%, having fallen to only 2.5% in the third quarter following on our New Economic Policy. The Government predicts that the rate of growth will rise to 5% if domestic stimuli currently being applied are successful, but this would still be substantially below the 10% growth rate to which the country has become accustomed over the past five years and more. Stock prices and new export contracts have declined sharply in the wake of our August 15 new economic program, and many Japanese firms are now reducing their investment plans.

Sato is trying to bring about this upturn principally through fiscal stimulation of domestic demand -- increased government infrastructure expenditures, adjustment of interest rates, and reduction of personal income taxes. To the extent he is successful, he will in addition to reviving the economic growth rate also reduce Japan's dependence on exports (now running at about 10% of GNP), and thus reduce his foreign policy problems. In the process, however, he is continuing to encounter several related economic problems, each of which generates its own political problems:

-- Infrastructure demands. There is rapidly growing pressure in Japan for long-delayed improvements in the quality of life and a faster rise in the general standard-of-living (at the expense of investment). Although a part of government infrastructure expenditures will stimulate new investment and production, a sizable proportion will be in the educational, social, and cultural fields, which will detract from immediate additions to the economic growth rate.

-- Industrial realignment. Japan is moving away from labor-intensive toward high technology industry -- a prominent example of

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which is textiles -- which puts a squeeze on both business and labor in the fields being phased out. On the other hand, the more Japan moves into high technology and depends on export markets in doing so, the greater her frictions with other high technology nations such as ourselves.

-- Foreign economic pressures. Even though Sato is stressing the stimulation of domestic demand, Japan cannot make the shift quickly enough to avoid current and possibly growing pressures from ourselves and other nations whose home markets are being penetrated by still expanding Japanese exports and investment. Foreign pressures on Japan are exacerbated in such cases as our own where foreign business and industry does not have equal access to the Japanese market.

Japan is beginning to make its peace with and adjust to the effects of our new economic policy, the emotional intensity of the initial Japanese reaction to our program having largely passed. Japan's larger firms are sufficiently competitive to maintain satisfactory trade levels, although smaller firms in the more traditional labor-intensive industries appear to be badly hit. The long-festering textile question between us has been solved, and the government is helping this particular labor-intensive industry adjust through massive subsidies. The Sato Government is in the process of working out with us a resolution of the currency revaluation problem and the surcharge, and it is slowly responding to our pressures for liberalization of imports and investment. The latter will require a long-term reorientation of Japanese business philosophy, which is reinforced by an archaic marketing structure that disadvantages imports. Most important for Sato here will be that we, in maintaining steady pressures for a resolution of these basic bilateral economic problems, avoid applying this pressure through a succession of blunt ultimatums.

3. Succession as LDP President and Prime Minister.

Prime Minister Sato is vitally interested in controlling the third major problem before him -- succession to the LDP Presidency and therefore the Primeministership -- in order to try to insure the continuity of his policies and his continued influence in the government and party (his current term as LDP President does not actually end until November 1972). His choice is Foreign Minister Fukuda. Sato can probably swing this succession if (a) he promises Minister of International Trade and Industry Tanaka that he will support Tanaka for the

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Prime Minister post at a future date, and (b) Tanaka is willing on this basis to throw his support to Fukuda rather than former Foreign Minister Ohira. (Ohira rather than Fukuda as Prime Minister, however, would not be likely to make a significant difference to our relationship.)

The Embassy and State continue to believe that we would affect the succession question only if a contretemps were to develop between us that resulted in Sato's resignation. This could scotch Fukuda's chances and incline Sato's successor toward more independent policies vis-a-vis our own. I would argue that this does not constrain what we do as regards Japan in the areas of economic relations and China policy nearly so much as how we do it -- that we not leave Sato stranded at home politically in the way we broach initiatives, and that we avoid applying our pressures through blunt ultimatums.

Concurrence:
Mr. Hormats

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